

The following is the transcript of debate on Chris 2003 amendment to H.R. 2420.

SHAYS: Thank you, Mr. Chairman. I have an amendment at the desk. I would like the amendment read.

OXLEY: Without objection, that will be the case. The clerk will report the amendment.

CLERK: Amendment offered by Mr. Shays. After section 9, insert the following new section and redesignate the succeeding section accordingly. Section 10, deceptive or misleading names. Not later than 270 days after the date of enactment of this Act, the commission shall prescribe, pursuant to section 35(d) of the Investment Company Act of 1940, a rule prohibiting unregistered investment companies from using the words "federal, federally, government, governmental" or specified variations thereof in the title of such company, or of any securities of which it is the issuer, unless not less than 80 percent of the portfolio of such company consists of securities that, one, are direct obligations of the United States or that are expressly guaranteed as to principal or interest by, or supported by the full faith and credit of the United States; two, are issued by a foreign government; or three, are issued by a state or local government.

OXLEY: The gentleman from Connecticut is recognized for five minutes in support of his amendment.

SHAYS: Thank you, Mr. Chairman. Mr. Chairman, this amendment, as you heard, direct the Securities and Exchange Commission to issue a rule prohibiting mutual funds from using the words "federal" or "government" in their names, unless at least 80 percent of their portfolio consists of securities that are direct obligations of a government. The amendment prevents mutual fund investors from being misled by fund names that suggest the funds invest extensively, particularly in U.S. government securities, when in fact they are largely invested in the securities of private corporations.

Two weeks ago, the Wall Street Journal ran an article exposing the significant abuse in this area. According to a well known researcher, Morningstar, Inc., 182 bond funds with about \$180 billion in assets had more than one-third of their assets in **Fannie Mae** or Freddie Mac as their most recent filings, even though their fund names did not mention mortgages or Fannie or Freddie themselves. More than 80 bond funds invested at least half their assets in Fannie and Freddie debt, and 74 of those funds used the words "government" or "federal" in their names.

The Lord Abbott Limited Duration U.S. Government Securities Fund, for example, had an astonishing 85 percent of its assets in Fannie and Freddie debt, or mortgaged-backed securities guaranteed by these two companies. Fannie and Freddie Mac are not backed by the full faith and credit of the United States. This amendment does not direct any mutual fund to change its investment objective or shift its funds from one asset to another. Rather, this amendment simply states that funds should be named in a manner that does not give investors the impression they are government-backed, when in fact they are not. Most investors should rightfully expect a government fund to primarily invest its assets in treasury bills and other government-backed securities, not the securities of private companies.

Finally, my amendment directs the SEC to promulgate, as consistent with existing SEC guidelines on mutual fund names. As my colleagues may know, the SEC recently changes the rules that apply to mutual fund names in order to ensure that fund names more accurately reflect the assets in which they are invested. According to these requirements, if a fund calls itself "electronics" funds, it is required by the SEC to invest 80 percent of its portfolio assets in electronic companies. If a fund calls itself the "small cap" fund, it is required to invest 80 percent of its assets in small cap companies. The same should be true for so-called "government" funds. This amendment is in keeping with the SEC recently adopted rule, and I urge my colleagues to support it.

I yield back, Mr. Chairman.

OXLEY: The gentleman yields back. Is there further discussion on the amendment? The gentleman from Pennsylvania is recognized for what purpose?

KANJORSKI: To strike the last word.

OXLEY: The gentleman is recognized for five minutes.

KANJORSKI: Mr. Chairman, I sympathize with the position of my friend from Connecticut because I myself think in some instances names of entities are misleading. But we are sort of closing the box after there has been an escape, and I am not sure how we can go back and do that. I think the thrust of the amendment, maybe I direct it to my colleague from Connecticut, the thrust is to not have an entity known as a federal fund able to purchase Freddie and Fannie securities, because they are not supported by the full faith and credit of the United States government. There is no denial that they are quasi-governmental agencies, licensed, chartered, whatever you will, as government-sponsored enterprises. It seems to me that if they do not meet the standard test that 80 percent of the portfolio consists of, quote, "government securities," they cannot use those titles. The punishment is you have to change your name.

Now, I see that my colleague from Connecticut has joined state and local governments, and I suggest a fund that buys municipal authority bonds is not getting a bond that has the full faith and credit of that municipal government. That is why we create authorities, both on the state level and the municipal level, so they have the capacity to sell unguaranteed with the full faith and credit of the locality or the local government.

So we build illogically into the statute a contradiction. What we are trying to do is stop funds from claiming they are federal or governmental funds so they cannot buy Freddie and Fannie, or get penalized, but they can go out and buy municipal authorities. The Kokomo municipal authority bond is OK, even though that does not have the full faith and credit of the community.

SHAYS: Would the gentleman yield?

KANJORSKI: Certainly.

SHAYS: Two points. First, they could continue to invest in Fannie and Freddie, but they could not call themselves a government fund. So just to put that on the record. They either change their name or they change their investment portfolio. Secondly, we are asking the SEC to draw the regulations to deal with the kind of issue that you are bringing up.

KANJORSKI: And I appreciate it.

SHAYS: So there will be a comment period. They can take two years to have it take effect. They can do a number of things.

KANJORSKI: The question is in my mind, do we want to stop the flexibility and availability of the larger market for state and municipal authority bonds in this country, because we are worried about investors making the mistake that this is in some way a U.S. government entity that is selling these bonds? Again, it goes to the issue of what are we protecting here. Have we had a lot of investors come forward and tell us that they have been wiped out or lost a lot of money because somebody misrepresented to them that they were a federal mutual fund? If so, is it our obligation? I mean, you are a pretty stupid investor if you do not understand what the fund you are putting your money in is made up of or what its authority is.

I do not know that we have the obligation to protect the fourth standard deviation from the norm. I think our obligation is trying to keep an aggressive field and an aggressive market. Here what we are doing potentially, the unintended consequences, is that if a fund were to be a major acquirer of municipal authorities or state authorities, that did not have the full faith and credit of their various state governments, that that would count against them in the formula, and that would be incredible to collapse or implode that tremendous vital market in the United States for infrastructure that is huge, tens of billions, fifties of billions of dollars a year.

SHAYS: Will the gentleman yield?

KANJORSKI: Yes, I will.

SHAYS: Thank you. This legislation that we are dealing with, and it is interesting admittedly that it seems to be coming more from the Republican side than the Democratic side of the aisle. There are two issues we are trying to deal with. We are trying to deal with conflict of interest. We are trying to deal with truth in advertising. So basically, it would be the same kind of question that you asked. What are we trying to deal with?

A few years ago, I argued that auditing firms should be allowed to do consulting services, and I gave the same argument you did. Where is the problem? What are we trying to deal with? And then this committee had a hearing, and we learned that Arthur Andersen had \$25 million of Enron consulting and \$28 million of auditing. And we realized there was a problem. So let's deal with it now and not later.

KANJORSKI: We are not dealing with an issue that has changed now. We are dealing with what the ranking member suggested we maybe doing. We are targeting the mutual fund industry. If we are to look at how this role applies, why shouldn't we ask the question of whether you could use "national" bank in your name? Why should we allow federal credit unions to advertise as federal credit unions? I do not think anybody in this country is stupid enough to think that if they belong to the ABC Federal Credit Union that it is an entity of the United States government. If they are, maybe they should enlarge their mattress.

(LAUGHTER)

OXLEY: The gentleman's time has expired. Who seeks recognition? The gentleman from Delaware seeks recognition for what purpose? The gentleman is recognized for five minutes.

CASTLE: Thank you, Mr. Chairman. I would like to pose questions to the gentleman from Connecticut. First of all, I just opened up a Wall Street Journal. I looked through this and there are a lot of GNMA funds. I don't know if that is what their real name is, or if it is Government National Mortgage Association-held securities funds or what it is. They would be eliminated from being able to call themselves that. Is that correct? They would have to take the word "government" out of their title because it is not a government-secured fund necessarily?

SHAYS: If they are investing less than 80 percent in government entities, yes.

CASTLE: And you are saying the GNMA funds are not government funds.

KANJORSKI: They are supported with full faith and credit pledges.

SHAYS: Yes. I am sorry.

FRANK: If the gentleman would yield?

CASTLE: I will yield to anybody who can answer it.

KANJORSKI: If I may, I believe Ginnie Mae is supported with the full faith and credit of the United States government, as opposed to Fannie and Freddie.

CASTLE: OK. Are there funds with the name, I think this sounds like a good amendment, but I am concerned about you are going to get what you ask for and it could be a problem. I am concerned about, do we know that there are funds out there who will have to divest themselves of something and buy something else to get to the 80 percent? Can they do it in the 270 days?

SHAYS: First off, if I could. Would the gentleman yield?

CASTLE: Sure. I would be glad to yield.

SHAYS: The 270 days is the beginning of the regulation, and then there is a comment period and dialogue and so on. We are not drafting the rule. We are asking the SEC to draft the rule to consider all the kind of questions that you are asking. In terms of when the SEC thinks they could implement it, they could have it be a two-year or a three-year process for there to be a decision whether they want to keep their name or to change their portfolio.

KANJORSKI: Will the gentleman yield?

CASTLE: I will be glad to yield.

KANJORSKI: Let me point out the problem is see. The Franklin Federal Tax-Free Income holdings fund, if you look down their list of holdings it is Dallas-Forth Worth, Texas; it is Massachusetts state; it is New York, New York bonds; it is North Carolina Eastern Power Agency; it is Clark City development revenue bonds. All of these are municipal, governmental or state bonds that are sold through entities that do not pledge the full faith and credit of their respective governments. So an entity such as this would have a very limited period of time either to divest themselves of their holdings, which to a large extent are bonds that have long maturity and could cause them extraordinary losses if they had to dispose of them in a limited period of time, or change their name.

There is another one - the Janus Federal Tax Exempt Fund. That is the same thing.

CASTLE: Let me reclaim my time and ask the question, then, of the sponsor. For example, there are a lot of these funds in here that are municipal bond funds, or a municipal bond fund is in them, but they would not be regulated in the same way because that is not included by your amendment. Is that correct? Your amendment, it seems, includes "federal, federally, government and governmental," and you have something called a municipal bond fund, and it would seem to me it would be just as important it be a California municipal bond or a Pennsylvania municipal bond or whatever.

SHAYS: I must not be understanding the gentleman, because we are basically saying on point three, "are issued by a state or local government." What am I missing?

CASTLE: What you are missing is that you have a series of mutual funds in any of these families which have the word "municipal" in them. It seems to me it is equally as important to know that there are municipal bonds in those municipal bond funds. SHAYS: If the gentleman is asking whether we are dealing with "municipal," we are not dealing with that issue. So we are not making it as comprehensive as we could. That is correct.

FRANK: Mr. Chairman? Will the gentleman yield?

CASTLE: Let me just finish, if I may, and then I will be happy to yield. We do not have time to resolve this now, and I am not sure we are going in the right direction, but it seems to me that is an important issue because people buy those for tax-free reasons, and that may be as significant as anything we are doing.

SHAYS: If I could say to the gentleman, if he would yield me the time.

CASTLE: I would be happy to yield.

SHAYS: We decided to take a smaller bite of this, rather than a more comprehensive one, but I do not think you can fault the amendment for being not as comprehensive. This is a process that we would begin, and if we did more, I am sorry we did not do as much as you might want, but we did something.

FRANK: Mr. Chairman?

CASTLE: I would be happy to yield, if there is still time, to the gentleman from Massachusetts.

FRANK: I will wait for my own time. It's OK.

OXLEY: Does the gentleman yield back? The gentleman yields back. The gentleman from Massachusetts is recognized for what purpose?

FRANK: Mr. Chairman, I move to strike the last word.

OXLEY: The gentleman is recognized for five minutes.

FRANK: I have a couple of problems with the amendment. One, I think the gentleman from Connecticut has understated the extent to which this tells the SEC what to do. It does not leave them with much discretion. It says, not later than nine months after the date of enactment, they shall prescribe. Now, the rule could say it does not go into effect right away, but they shall prescribe a rule prohibiting them from using the words. So there really is not much flexibility here. They can talk about whether they give them seven or eight months or nine months to do it, but it is fairly prescriptive. It does not leave much to the SEC. So when he says the SEC will work it out, I think there is not much left for them to work out.

Secondly, I think he has a stronger point with the word "government" than with the word "federal." The word "federal" is used in a lot of contexts here. My guess is if we had a phone book and looked it up, we would find in the business section a lot of businesses called "federal." When I was growing up in New Jersey, the leading liquor wholesaler was Federal Wine and Liquors, and not many people thought it was the government.

OXLEY: What age were you then?

FRANK: What?

OXLEY: What age were you then?

(LAUGHTER)

FRANK: I was underage, but we did not have that in Hudson County, New Jersey.

(LAUGHTER)

Maybe the city had a piece of it, but I think "federal" and "government" are not the same thing.

There is one other problem I have here which is you can say "federal" if you are issued by a foreign government. Well, I suppose that would cover the Federal Republic of Germany, but I do not know that Ukraine is federated or Kazakhstan or other countries. Frankly, I think in that sense it is too much to give people. Oh, don't worry, these bonds are issued by Uzbekistan, which the bill would allow, I think would be a mistake.

I understand the gentleman has concerns about **Fannie Mae** and Freddie Mac, and I think those are things that we should be dealing with frankly in their own context. But I do think that "government" I could agree with, and if we got a later chance to look at this, I do not think people ought to be able to advertise themselves as selling government bonds unless they are government, and I would say federal, state or local full faith and credit. I would not put foreign governments in there because they may or may not be full faith and credit of the foreign government. The foreign government may not have any real credit. But "federal" does concern me, and I really do believe that we have many entities in this society that say "federal" and I do not think that has always meant the same.

So for that reason, I would not vote for this now. I would be willing to work on something to come up later that would say you cannot advertise yourself as a government fund. You should not be able to give the implication that you are tax exempt when you are not. You should not be able to use "government," but the purpose of involving foreign government here and having "federal" in there, one goes too far and one does not go far enough for me.

OXLEY: The gentleman yields back. The gentleman from Pennsylvania has been waiting patiently. I recognize the gentleman from Pennsylvania for what purpose?

MURPHY: To strike the last word.

OXLEY: The gentleman is recognized for five minutes.

MURPHY: I have a question for the gentleman from Connecticut, too. We have a rather large and respected company that has many mutual funds in Pittsburgh, called Federated Investors. In the wording here where it says "variations thereof" in the title of such a company, I would think that they would be quite worried right now that that might be changed. Plus, many of their funds have that in as well. I also was checking out the Wall Street Journal and looking at all the funds listed, and many are government ones, and I would hope that, like the gentleman from Massachusetts said, we would find some other way.

I think I understand what you are trying to get at there, and I am sympathetic to it, because no one wants to see investors duped into investing in something that is not what they wanted. But I would be concerned about trying to dictate the title of things here.

I yield back.

OXLEY: The gentleman yields back. Is there further discussion?

NEY: Mr. Chairman?

OXLEY: The gentleman from Ohio, Mr. Ney, is recognized for what purpose?

NEY: Thank you, Mr. Chairman. I seek to strike the last word.

OXLEY: The gentleman is recognized for five minutes.

NEY: Thank you, Mr. Chairman. I want to voice opposition. I hate to do that, not that we have not opposed each other before when we try to find something that we can work on and I will agree on, Mr. Shays. But I want to voice opposition to the amendment. While it is well intended, and I do believe in the sincerity of the gentleman I have never questioned, I do believe it is unnecessary and burdensome, and I think it can be indirectly detrimental.

I think it is important that members know that the rule is completely redundant. The SEC in early 2001 updated its rules on what funds must hold in relationship to their names. After exhaustive study, they did not feel it was necessary to change what government funds hold, so I do not see why we need to do that now at this point in time.

Furthermore, what is offered in the government agency debt market is controlled by the Treasury Department, and they have been comfortable with the GSEs operating in that market. Treasury, after close examination, felt it was proper for GSE and government debt to trade in the same markets. Again, I stress after close examination. So I think what we have here really is an amendment that is really a solution in search of a problem. We have yet to see any funds run into difficulties because they hold GSE debt. Thanks to the safety and soundness oversight of this committee and Chairman Baker, I believe we have no reason to believe there will be a problem necessarily in the future.

This is nothing more than I think an indirect, not intentioned, but indirect problem an assault on homeownership. What this amendment would do is merely force hundreds, if not thousands of funds to restructure their investments, or change their names and all their supporting literature for essentially no benefit to the investors. This amendment could force fund managers to restructure their portfolios because of new naming rules. The possible forced divestiture of GSE debt could be devastating for homeownership at a time when we can least afford to have our nation's housing market weakened. We know we are in a tough economy right now. The only saving grace in the last couple of years have been houses, homeownership and cars. And right now, cars are not having that same benefit. So it is all up to homeownership.

Our nation's economy is finally starting to show hopefully signs of recovery, and I think we are going to dramatically at the wrong time rewrite the rules for funds that provide the resources GSEs use to invest in homeownership. So I do not see the point in doing the amendment when there has been no indication there is a problem at all, and I just think it is unnecessary, and could be, although not intended in this direction, but it could be potentially harmful. That is why I would be respectfully opposing the amendment.

OXLEY: The gentleman yields back. Is there further discussion? The gentleman from Pennsylvania, Mr. Toomey, is recognized for what purpose?

TOOMEY: To strike the last word.

OXLEY: The gentleman is recognized for five minutes.

TOOMEY: Thank you, Mr. Chairman. I would like to start by associating myself with the comments of my colleague from Pennsylvania. I share his concern very much with regard to a very large firm based in the western part of Pennsylvania that might be very concerned by this amendment.

While I understand, and I think there is a legitimate argument that the gentleman from Connecticut makes about being truthful in advertising, I think there could be some unintended consequences. So I would agree with the gentleman from Massachusetts that maybe we ought to try to work out a different approach to this. For instance, one of my concerns is as I read this amendment, you could not describe a fund as a fund of government-sponsored enterprise securities, but yet we all call **Fannie Mae** and Freddie Mac and a number of other institutions, we describe them as GSEs. They are universally known as GSEs. That term has a meaning which we all understand. I do not think it is misleading at all. But yet the word "government" being in this amendment would seem to me would preclude the possibility of describing such a fund in a perfectly accurate way.

I suspect that may not be the intent of the gentleman from Connecticut. So my suggestion would be that we go at this a slightly different way, because I think the wording here is a little misleading.

I would be happy to yield. I yield.

OXLEY: The gentleman yields back. The question now occurs on the amendment of the gentleman from Connecticut. SHAYS: Would the gentleman yield?

TOOMEY: Of course. I would be happy to yield.

SHAYS: I thank the gentleman. I get the sense that this amendment does not have much support, but I would like to put it on the record because I know we will be back, if in fact my intuition is correct. I want to put on the record that clearly this would impact mostly **Fannie Mae** and Freddie Mac. I want to put on the record that unless some people have been in another country, to say that there is no indication of any problem would belie the fact that Freddie Mac has basically said that they do not know how much they have earned; they have understated their earnings to the tune of \$1 billion to \$4 billion, which would probably mean that they have not paid their proper taxes and so on.

We know that **Fannie Mae** and Freddie Mac are far more leveraged. This is a warning I feel to all of you. You may be in the circumstance I was when it was with consultants. I remember defending the fact that accounting firms should be able to do consulting work. And I remember writing a letter to the SEC and saying this should happen. And I had the head of the SEC call me up and say, "Chris, you are wrong. We do not need more time to think this issue through." And he was right. I went to the floor and said I am not asking for more time, and he was right. And we saw Enron. And we are looking at **Fannie Mae** and Freddie Mac square in the face and acting like there is not a problem. You have people who believe that when they invest in these funds, they are backed by the federal government. They are not.

And so I am fully prepared to lose this amendment. I am not going to withdraw it and I will not ask for a roll call vote, but I think we will be back, and I do not think it is going to be written much different from this when it finally passes.

Thank you for yielding to me.

OXLEY: The gentleman yields back. The question now occurs on the amendment offered by the gentleman from Connecticut. All those in favor signify by saying aye.

Those opposed, no.

In the view of the chair, the noes have it. The noes have it and the amendment is therefore not agreed to.